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Supreme Court of the United States

OCTOBER TERM, 1927.

No. 48

ALEXANDER LATZKO, *et al.*, trading as Latzko & Popper,
Petitioners,

against

THE EQUITABLE TRUST COMPANY OF NEW YORK, as Trustee in Bankruptcy of Knauth, Nachod & Kuhne,
Respondent.

No. 49

THE EQUITABLE TRUST COMPANY OF NEW YORK, as Trustee in Bankruptcy of Knauth, Nachod & Kuhne,
Petitioner,

against

ALEXANDER LATZKO, *et al.*, trading as Latzko & Popper,
Respondents.

BRIEF FOR RESPONDENT-PETITIONER

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THE EQUITABLE TRUST COMPANY OF NEW YORK, as Trustee in Bankruptcy, etc., Petitioner, *against* ALEXANDER LATZKO, *et. al.*, Respondents.	No. 49

Brief for The Equitable Trust Company of New York, as Trustee in Bankruptcy.
Respondent in No. 48.
Petitioner in No. 49.

Statement.

Two writs of certiorari were granted by this Court to review the determination of the Circuit Court of Appeals for the Second Circuit. In both cases Alexander Latzko,

et al. in their brief refer to themselves as "petitioners" and to The Equitable Trust Company of New York, Trustee in Bankruptcy, as "respondent." For convenience that terminology has been adopted in this brief. The italics throughout this brief are inserted by counsel, unless otherwise noted.

The relation of these Cases to No. 34. The Equitable Trust Company of New York, etc., Petitioner, v. Carl Rochling, et al, Respondents.

Essentially the present cases present the same questions as are presented in No. 34, viz., whether prior to the filing of the petition in bankruptcy the bankrupts acquired title to certain checks received by them on June 15th, 1923, the day before the filing of the petition in bankruptcy, or whether the checks were received only for collection, with the result that the proceeds of the checks collected from the drawer after the bankruptcy belong to the petitioners. There are certain differences in the facts between these cases and that of *The Equitable Trust Company* vs. *Rochling*, No. 34, but it will be shown that the same principles must control the disposition of all the cases.

The Facts.

The petitioners, who are international bankers with headquarters in Hungary, maintained an ordinary checking account with the bankrupts (fol. 81).

Goldman, Sachs & Company Check.

On June 15th, 1923, the day prior to the filing of the petition in bankruptcy, the petitioners "caused" (fol.

22) Goldman, Sachs & Company to deliver the latter's check to the bankrupts for $15,000 drawn on the Bank of America payable to the order of the bankrupts. That check was accompanied by a separate communication that the check was "for account of Latzkopper Budapest" (fols. 91, 92). On receipt of the check on June 15th the bankrupts promptly credited petitioners' account with the amount thereof (fol. 93) and in turn deposited the check in the regular course of business with the American Exchange National Bank, being thereupon on that same day (fol. 94) credited by the American Exchange National Bank with the amount thereof. On June 16th, after the filing of the petition in bankruptcy, the check passed through the New York Clearing House and was paid (fol. 95). Copies of the check and of the accompanying communication from Goldman, Sachs & Company to the bankrupts are set forth at length in the Master's Opinion at folios 91 to 93.

The National City Bank Check.

Also on June 15th, 1923, the petitioners "caused" (fol. 22) the National City Bank to deliver to the bankrupts its cashier's check for $1,294 payable to the order of the bankrupts "favor N. Latzko and A. Popper, Budapest." A copy of the check is set forth at length in the Master's Report (fol. 88). On receipt of this check on June 15th the bankrupts promptly credited the petitioners' account with the amount thereof and deposited the check in the regular course of business with the American Exchange National Bank being thereupon in turn credited by that

bank with the amount thereof (fols. 89, 90). On June 16th, after the filing of the petition in bankruptcy, the check passed through the New York Clearing House and was paid (fol. 90).

Facts Relating to Both Checks.

After the bankruptcy an indebtedness of the bankrupts to the American Exchange National Bank was in part satisfied by the application of the bankrupts' balance, as increased by the two deposits above referred to, and, thereafter, certain collateral held by the bank against the indebtedness was returned to the Receiver. It is against the proceeds of this collateral that the petitioners here file their reclamation claims.

Other Important Facts Applicable to Both Checks.

1. It is to be emphasized with respect to each of the two checks that the reclamation petition (fols. 22, 23) alleges, and the allegations stand admitted, that the petitioners herein "*caused*" Goldman, Sachs & Company and the National City Bank to deposit said checks for petitioners' account with the bankrupts. The legal effect of this fact is held by the courts below to be the same as though the petitioners had themselves deposited checks for their own account (fol. 252).

2. There is no evidence of any special agreement between the petitioners and the bankrupts with respect to the treatment of checks which petitioners caused various banks or bankers to deposit with the bankrupts in the manner above described.

3. Although it was admitted by the respondent that as a matter of fact petitioners had not theretofore drawn against their account with the bankrupts before checks deposited had been actually collected, there was no evidence offered to show that the petitioners did not have the *right* to draw before the checks were actually collected. While it is true, therefore, as stated by petitioners at page 5 of their brief that "the petitioners had no agreement with the bankrupt to treat evidences of debt, deposited with them for collection or otherwise, as a deposit of cash," there was also no agreement that petitioners' deposits were *not* to be treated as cash or that petitioners *could not* draw against deposits until after their collection. As the Master said (fol. 103):

> "* * * the burden is on the petitioner to prove a special agreement showing that it had *no right* to draw before collection."

Erroneous Statement of Fact in Petitioners' Brief.

There is no basis in the Record for the statement on page 3 of petitioners' brief that the bankrupts delivered the checks in question to the American Exchange National Bank "for collection." The very pages of the Record, 30 and 32, referred to by petitioners show that the bank credited the checks to the bankrupts' account immediately on their receipt. No mention is made anywhere of "collection."

Material Distinctions of Fact Between These Cases and The Rochling Case, No. 34.

1. In the *Rochling* case, *all* of the checks were payable

on their face to the order of the bankrupts "for account of" Rochling. In the present case the check of the National City Bank for $1,294 was similarly payable on its face to the order of the bankrupts "fa[illegible] of Latz-Kopper." But the check of Goldman, Sachs & Company for $15,000 was on its face simply payable to the order of the bankrupts and the information that it was paid to the bankrupts for the account of the petitioners was conveyed *in a separate accompanying communication.*

2. In the *Rochling* case, the reclamation petition did not specifically allege that Rochling had "caused" the deposit of the checks, as petitioners did allege in the present cases. But the correspondence between Rochling and their London correspondents indicated that in fact Rochling had caused the deposit to be made. The petitioners here point out that in the *Rochling* case, Rochling was credited with interest from the date that the checks were received for their account by the bankrupts. Petitioners here add (p. 8 of their brief) that they "received nothing on their deposits." *There is no evidence in the Record as to whether or not the petitioners in this case received interest. If the petitioners deemed it material to show that they received no interest, the burden was upon them to prove that fact.*

3. In order to complete the distinction of fact the respondent points out that the *Rochling* case was further strengthened by the appearance of the fact that Rochling desired credit for the amount of the checks transmitted to the bankrupts on a definite date, i. e. June 15th, and contracted with their correspondents for the payment on

that date. While such facts do not affirmatively appear in the Record in the present cases—in fact there is no evidence at all on the subject—it is to be presumed that international bankers dealing in transfers of large credits are at all times aware when they may expect credits to be placed to their account and to be made available for their use.

4. Certain other differences, pointed out by petitioners at pages 7 and 8 of their brief, exist but have no materiality; i. e., that the Goldman Sachs check of $15,000 was not a cashier's check; and that there was no evidence as to whether Rochling ever drew against their balances before collection of deposits. Why the legal rights of the parties are different in the case of the Goldman Sachs check, drawn upon another bank, than in the case of the National City Bank's cashier's check is not pointed out. And as to the absence of evidence of whether Rochling ever drew against its balance before collection of deposits, it need only be pointed out that the fact as to whether or not there *was* ever a drawing before collection *is immaterial, the only material question being whether a right to draw existed.*

Holdings Below and the Fundamental Error.

In all the cases, and with respect to all checks, the Special Master and the District Court concurred in holding that there was no reclamation rights because title to the checks had passed to the bankrupts on delivery on June 15, 1923. In the Circuit Court of Appeals it was held that the bankrupts did *not* take title on June 15,

1923, to the checks which were payable on their face to the order of the bankrupts "for account of Gebreuder Rochling" and "favor of Latzkopper" but that the bankrupts *did* take title to the Goldman Sachs check which was payable simply to the order of the Bankrupts despite the fact that there was an accompanying statement that the payment was made "for account of Latzko and Popper."

The Circuit Court of Appeals made the form of the face of the check the test. (Record in No. 34, page 36).

The basis of the Circuit Court of Appeals' distinction based on the form of the check is found in its reasoning that when the words "for account of" or "favor of" appear on the face of the check, notice is given to a third party endorsee of the capacity in which the bankrupts hold the checks, whereas when such notation does not appear on the face of the check, though it was given to the bankrupts with an accompanying instruction, the third party has no notice of the capacity in which the bankrupts held the check. *The fundamental error in this reasoning is that the only relationship in question here is that existing between the bankrupts and their depositors, Rochling in the one case, and Latzko in the other. The rights of third parties, endorsees from the bankrupts, are not here presented. The effect of notice to such endorsee is immaterial. The only question presented in all of these cases is what was the relationship* AS A FACT *between the bankrupts and their depositors.* Was the transaction such that in the absence of any special agreement the deposit of the checks with the bankrupts for account of their depositors passed

title to those checks to the bankrupts, as in the ordinary case of a deposit of checks by a depositor with his bank, under the rule of this Court's decision in *United States* vs. *Burton*, 196 U. S., 283. Whether or not a third party endorsee of the checks which on their face are payable for account of the depositor would be put upon notice as to what in fact was the relationship between the payee and its depositor is not the question presented. But even if the rights of a third party endorsee were here in question and he were held to be put on notice as to the nature of the relationship between the payee bank and its depositor, *it would still be a matter of fact to be proved as to what that relationship was.* Here an investigation by an endorsee would have resulted in the discovery that the relationship between the payee banker and its depositor—Rochling or Latzko—was after the credit of the checks, simply that of debtor and creditor, thus enabling the bankrupts to give to the third party endorsee good title to the checks. *Since, however, an endorsee's rights are not here involved, the Court need go no further than to determine the nature of that initial relationship between the bankrupts and their depositor.*

In the case where the Court correctly interpreted the problem as that of the relationship between the bankrupts and their depositors, i. e., in the case of the Goldman Sachs check for $15,000, the Court concluded, in accordance with respondent's contention, that the relationship existing was one of debtor-creditor. It was only when the Court became confused by considering the rights of possible third party endorsees that the Court measured the rights of the petitioners here by the form

of the check. The respondent contends that the relationship between the bankrupts and their depositors in all of the cases was the same as that which arose upon the delivery of the Goldman Sachs check and its credit to the account of the depositor.

POINT I.

As between the bankrupts and their depositors, the petitioners, the capacity in which the bankrupts received the two checks which the petitioners "caused" to be delivered to them for the petitioners' account depends upon the intention of the bankrupts and the petitioners. Under the rule of the Burton case the presumption is that those parties intended to create a debtor-creditor relationship. There is no evidence here to rebut that presumption.

The petitioners themselves alleged, and the Courts below have found as a fact, that the petitioners had "caused" Goldman, Sachs & Company and the National City Bank to deliver their respective checks to the bankrupts. As a result the conclusion was reached that "the legal effect of the transaction was the same as though the petitioners had themselves deposited the check 'for our account' with the bankrupts on June 15th and the latter had at once credited it to the petitioner" (fol. 252). Since the result of the petitioners' causing the checks to be deposited is the same as if they themselves

had deposited checks to their own credit with the bankrupts, the question presented here is the same as that raised in this latter situation.

A.

General Presumption in Favor of a Debtor-Creditor Relationship.

Of course the relationship ordinarily existing between the bank or banker and its depositor is that of debtor and creditor, and not principal and agent, or trustee and *cestui*. Since the leading cases of *Foley* vs. *Hill*, 2 H. L., 28, and *Bank of Republic* vs. *Millard*, 10 Wall., 152, this relationship has been recognized. In the latter case, this Court said:

> "It is an important part of the business of banking to receive deposits, but when they are received *unless there are stipulations to the contrary, they belong to the bank, become part of its general funds, and can be loaned by it as other moneys.* The banker is accountable for the deposits which he receives as a debtor, and he agrees to discharge these debts by honoring the checks which the depositor shall from time to time draw on him. The contract between the parties is purely a legal one, and has nothing of the nature of a trust in it. This subject was fully discussed by Lords Cottenham, Brougham, Lyndhurst and Campbell in the House of Lords in the case of *Foley* vs. *Hill*, 2 Clark & Finnelly, 28, and they all concurred in the opinion that the *relation between a banker and customer, who pays money into the bank,* OR TO WHOSE CREDIT MONEY IS PLACED THERE, *is the ordinary relation of debtor and creditor,*

> *and does not partake of a fiduciary* character, and the great weight of American authority is to the same effect."

Whether, therefore, the *depositor* sends *moneys* to his banker, or money is sent *for his account* by third parties, by the depositor's direction or with his knowledge, the title to the money passes to the banker and simultaneously therewith there springs up a debtor and creditor relationship between the banker and his depositor.

The foregoing general rule of *Foley* vs. *Hill* and *Bank of Republic* vs. *Millard* as to the effect of the deposit of *money* by the depositor himself has been extended by the leading cases in this Court and in New York to the deposit of *checks* and other instruments by the depositor himself where the deposit has not been made under special circumstances or in pursuance of a special agreement showing that a different relationship, in fact, was *intended* to be created. Thus in *Cragie* vs. *Hadley*, 99 N. Y., 131, quoted with approval by this Court in *Burton* vs. *United States* (1905), 196 U. S., 283, at 302, the New York Court of Appeals said:

> "The general doctrine that upon a deposit being made by a customer, in a bank, in the ordinary course of business, of money, *or of drafts or checks received and credited as money*, the title to the money, *or to the drafts or checks*, is immediately vested in and becomes the property of the bank, is not open to question. (*Commercial Bank of Albany* vs. *Huges*, 17 Wend., 94; *Metropolitan Nat. Bank* vs. *Loyd*, 90 N. Y., 530). The transaction in legal effect is a transfer of the money, or drafts or checks, as the case may be, by the cus-

> tomer to the bank, upon an implied contract on the part of the latter to repay the amount of the deposit upon the checks of the depositor. The bank acquires title to the money, drafts or checks, on an implied agreement to pay an equivalent consideration when called upon by the depositor in the usual course of business."

In *Metropolitan National Bank* vs. *Lloyd*, 90 N. Y., 530, quoted with approval in the *Burton* case, the New York Court of Appeals said:

> It is true no express agreement was made transferring the check for so much money, but it was delivered to the bank and accepted by it, and the bank gave Murray credit for the amount, and he accepted it. That was enough. The property in the check passed from Murray and vested in the bank. He was entitled to draw the money so credited to him, for as to it the relation of debtor and creditor was formed and the right of Murray to command payment at once was of the very nature and essence of the transaction. On the other hand, the bank, as owner of the check, could confer a perfect title upon its transferee, and, therefore, when by its directions the plaintiff received and gave credit for it upon account, it became its owner and entitled to the money which it represented. * * * If, as the appellant insists, the check had been deposited for a specific purpose—for collection, the property would have remained in the depositor, *but there is no evidence upon which such fact could be established, nor is it consistent with the dealings between the parties, or with any of the admitted circumstances.*

> "These show that it was the *intention* of both parties to make the transfer of the check absolute, and not merely to enable the bank to receive the money upon it, as Murray's agent."

In the *Burton* case (1905), 196 U. S., 283, the doctrine of the foregoing cases was approved, and this Court said:

> "There was no oral or special agreement made between the defendant and the bank at the time when any one of the checks was deposited and credit given for the amount thereof. The defendant had an account with the bank, took each check when it arrived, went to the bank, indorsed the check which was payable to his order, and the bank took the check, placed the amount thereof to the credit of the defendant's account, and nothing further was said in regard to the matter. In other words, it was the ordinary case of the transfer or sale of the check by the defendant and the purchase of it by the bank, and upon its delivery to the bank, under the circumstances stated, the title to the check passed to the bank and it became the owner thereof. It was in no sense the agent of the defendant for the purpose of collecting the amount of the check from the trust company upon which it was drawn. From the time of the delivery of the check by the defendant to the bank it became the owner of the check; it could have torn it up or thrown it in the fire or made any other use or disposition of it which it chose, and no right of defendant would have been infringed. * * There was nothing whatever in the evidence showing any agreement or understanding as to the effect of the transaction be-

> tween the parties—the defendant and the bank—making it other than such as the law would imply from the facts already stated."

And further:

> "There was no agreement or untaking of any kind other than such as the law makes from the transaction detailed, which was itself proved by uncontradicted evidence offered by the Government itself. In the absence of any special agreement that the effect of the transaction shall be otherwise (and none can be asserted here), there is no doubt that its legal effect is a change of ownership of the paper, and that the subsequent action of the bank in taking steps to obtain payment for itself of the paper which it had purchased can in no sense be said to be the action of an agent for its principal, but the act of an owner in regard to its own property."

The doctrine of the foregoing cases has recently been applied by this Court in *City of Douglas* vs. *Federal Reserve Bank of Dallas*, 271 U. S., 489.

Compare the facts as stated by this Court in the *Burton* case with the facts in the present case. *In neither case was there any special agreement covering the deposit of the checks.* This Court in the *Burton* case emphasized that fact. In both cases the depositor had an account with the bank and in both cases checks were deposited therein. In the *Burton* case the check was deposited by Senator Burton himself, in the present case "the banks delivering these checks to Knauth, Nachod & Kuhne * * * were acting as agents of the petitioner, and the delivery of the checks to Knauth, Nachod &

Kuhne was the same as if they had been delivered by Latzko & Popper themselves" (fol. 102). In both cases the bank placed the amount of the checks to the credit of the depositor immediately upon the deposit of the checks (fols. 86, 89, 93). In both cases nothing further was said in regard to the matter.

This Court's conclusion in the *Burton* case is inevitable in the present situation—"it was the ordinary case of the transfer or sale of the check" by the petitioners through their agents and the purchase of the check by the bankrupts, and, on delivery to the bankrupts, title to the checks passed and there existed an indebtedness from the bankrupts to the petitioners for the amounts thereof.

Since the rule that the deposit of *money* by the bank's customer in the absence of a special agreement creates a debtor-creditor relationship has been extended to cases where *checks* are deposited by that customer, there is no reason why the same rule when applied to *money* deposited by third persons for the account of the depositor, should not likewise be extended to the deposit of *checks* by such third persons, *particularly when made pursuant to the depositor's direction as in the present case.*

The true test must be in all cases: Is there any evidence to show that as between banker and depositor a different relationship was intended to be created.

Of course, varying circumstances have been held sufficient to indicate that the relationship between banker and depositor was not *intended* to be that of debtor and creditor upon the deposit of checks, and that the relation-

ship was *intended* to be that of bailor and bailee, or principal and agent. Thus when a payee of a check *endorses* it to his banker *"for collection and credit,"* these words indicate that the payee-endorser does not intend to deposit the check, but intends only to constitute the banker his agent for collection and intends that the amount thereof should only be credited to depositor's account when the instrument is collected, and that then and then only should the relation of debtor and creditor arise.

All of this is well established law, as are the decisions of the Courts in the numerous cases relied upon by the petitioners, all to the effect that by endorsements in varying restrictive forms, the payee-endorser does not *intend* to divest himself of title to the instrument, but intends to constitute the endorsee his agent for the purpose solely of collecting the check for the endorser's account. *In other words, as between endorser and endorsee, the words of restrictive endorsement are held to indicate the* INTENT *not to transfer beneficial title.*

Those cases are wholly inapplicable to the present situation. Here the legal relationship between the bankrupts and the petitioners with respect to the checks must depend not upon the mere chance that the same words were used here by a third party bank as are ordinarily used by endorsors to create an agency relationship, but must depend upon the intention of the bankrupts and the petitioners. In the absence of evidence to the contrary, that intention is presumed by the *Burton* case to contemplate a debtor-creditor relationship.

B.

There is no Evidence Here to Rebut the Presumption Established by the Burton Case.

Inasmuch as it has just been shown that the relationship between the banker and the depositor is presumed to be that of debtor and creditor, the burden of proof is upon the petitioners here (the reclaimants below) to establish that some other relationship, such as principal and agent, existed. The petitioners have failed to sustain such a burden. There is no evidence of any special agreement to rebut the presumption. There is no evidence of any absence of right to draw against their credit immediately upon its creation. There is no evidence of any kind that the relationship was other than that which presumptively exists or that there was anything in the relationship of the parties from which an intention could be gathered that the petitioners constituted the bankrupts their agents to collect checks which the petitioners themselves had "caused" the New York banks to deposit for their credit.

There is no reason why a Court should be astute to discover special agreements that the relationship between the parties was intended to be other than that usually existing between banker and depositor. If such special agreements as desired, they may be easily and clearly made.

C.

Petitioners in their Points V and VI have failed in their attempt to distinguish the present Case from the Burton Case.

At pages 48 and 49 of their brief, petitioners unsuc-

cessfully attempt to prevent the application of the rule of the *Burton* case to this case.

The first three allegedly distinguishing features —that in the *Burton* case the depositors "received personally checks", "personally endorsed" them, and "personally delivered" them to the bank—constitute factual differences, but not distinctions which require the application of a different rule of law. Petitioners nowhere attribute any materiality to them.

Petitioners' fourth "distinction" that "there was no physical possibility for petitioners to draw at once on the bankrupts" is not true, but is immaterial if true. Petitioners might have disposed of their credit with the bankrupts by cable. Even if they *did not,* it is no proof that they had no *right* to.

Petitioners' "distinctions" numbered 5 to 9 are on analysis but two; (*a*) that no agreement existed under which the bankrupts were authorized to purchase deposits made for petitioners' account and (*b*) that petitioners had no right to draw against their deposits until after collection. The first (*a*), is conclusively answered by the rule of the *Burton* case which *presumes* a purchase by the bank and imposes a duty of proving a special agreement to the contrary on the person relying on such an agreement. The second (*b*), that a special agreement has been show, has no basis in the facts:

> "the evidence *shows* that Latzko and Popper *did not,* in fact, draw against their account with Knauth, Nachod & Kuhne until the items deposited were actually collected, but the evidence *does not show* that they had *no right to* draw before that

> time, *and the burden is upon the petitioner to prove a special agreement showing that it had no right to draw before collection.*" (Opinion of Special Master, fols. 102, 103).

Just as in *In re Jarmulowsky* (S. D. N. Y., 1917) 243 Fed., 632, Judge Learned Hand held that a creditor-debtor relationship depended "upon the depositor's immediate and unconditional *right,* and not merely as a *favor,* to draw upon the deposit," so conversely the material question here is the petitioners' *absence of right* to draw, and not the mere fact, as proven, that they *did not.* Petitioners have failed to sustain the burden of proving the absence of such right.

In making their final "distinction," petitioners are relying not on a distinction *in fact,* but on an assumption of the very legal conclusion which is the object of their entire brief. They claim that in the *Burton* case, at the time of deposit, there were no "instructions restricting negotiability." There were none here.

> "The letter which Goldman, Sachs & Company sent with the draft simply amounted to an explanation to the persons to whose order it was drawn (the bankrupts) that it was to be placed in the account of petitioners." (Judge Rogers, fol. 252).
>
> "But here the deposit was in the claimants' ordinary checking account. Instructions to place it to such account emanating from them, *and due to the necessity of indicating for whom the check was received,* create a different situation from that in *White* vs. *Miners National Bank,* 102 U. S., 658, where the deposit was in a bank where there was

an endorsement for account of A to the order of a bank in which *A had no checking account.*" (Judge A. N. Hand, fol. 118).

"I cannot believe that one who deposits a check in his own bank, in which he has an account," (or "causes" his agent to make the deposit for him, as here) "with a notation that it is for his (the depositor's) account, means that the title of the checks is to remain in the depositor until the bank collect it." (Special Master Stephenson, fol. 104).

D.

In Reply to Petitioners' Argument.

The fact that respondent's contentions lead to the conclusion that the bankrupts would have been liable to the petitioners for the amount of the checks credited to petitioners' account even if the checks had not been paid by the drawers—Goldman, Sachs & Company and National City Bank—is admitted.

Of course, if the bankrupts purchased the checks and did not take them solely for collection by virtue of some special agreement, the risk of loss was on them. If the bankrupts had distrusted the responsibility of the drawers of the checks and had deemed it desirable to protect themselves against the drawers' failure to pay them, they could have simply refused to accept the checks other than for collection. But these were transactions between well known banking houses in the same city and the bankrupts could well accept these New York checks as money and this, it appears, was their practise.

It is of course well known that since the decision of

this Court in the *Burton* case, many of the banks throughout the country, in cases where they deem it necessary, have protected themselves from the application of the rule in that case by very definite special agreements found in passbooks or on deposit slips. These express agreements have, in many instances, become necessary because banks receiving checks drawn by persons whose responsibility is unknown to them have found it unwise to assume the risk flowing from the rule of the *Burton* case. In the present case, however, the bankrupts made no special agreement and did not credit the checks solely for collection for the obvious reason that they deemed checks of the National City Bank and Goldman, Sachs equivalent to cash, which they safely could credit and upon which they could assume the risk.

Conclusion to Point I.

Accordingly, it is submitted that unless varied by the single circumstance that the New York banks carried out their instructions to create a credit by in one case, drawing their check to the order of bankrupts "in favor of Latzkopper" and the other case by drawing their check to the order of the bankrupts and delivering the same accompanied by instructions that it was "for the account of Latzkopper," the ordinary rule must apply that the relationship of debtor and creditor was created from the time of the receipt and credit of the checks, which the petitioners caused these banks to deposit.

It is therefore submitted that the doctrine of *Foley* vs. *Hill* and *Burton* vs. *United States* is applicable and leads to the conclusion that the beneficial title to both

checks passed to the bankrupts on June 15, 1923, and that thereafter the petitioners were no more than general creditors of the bankrupts.

POINT II.

The Court below correctly held that the bankrupts acquired title to the Goldman Sachs check prior to the bankruptcy and that the words "for account of" appearing in the letter covering the transmission of the check to the bankrupts did not constitute the bankrupts agents for petitioners but constituted them merely debtors as in the ordinary case of banker and depositor.

Referring to the letter which accompanied the Goldman, Sachs check, the Court below said (fol. 252):

> "* * * The petitioners state they caused Goldman, Sachs & Company, as their agents, to deliver it. The letter which Goldman, Sachs & Company sent with the draft simply amounted to an explanation to the persons to whose order it was drawn, that it was to be placed in the account of the petitioners. This they did as the agents of the petitioners. The legal effect of the transaction was the same as though the petitioners had themselves deposited the check 'for our account' with the bankrupts on June 15th and the latter had at once credited it to the petitioners. * * * We think the transaction is governed by the rule laid down in the *Burton* case, and that the rela-

> tion between the petitioners and the bankrupts on June 15th, when this check was credited by the latter to the former, was that of creditor and debtor, and that the proceeds of this check when it was collected on June 16th did not belong to these petitioners."

This conclusion is obviously sound. By some method Goldman, Sachs & Co. had to inform the bankrupts why and for whose benefit the money was being paid, whatever the nature of that benefit. *The transaction required either some notation on the check or some accompanying memorandum.* How other than by the use of the words "for account" could Goldman, Sachs have indicated to the bankrupts the name of the firm having an "account" with them for whose benefit the check was being transmitted. *Even if the petitioners had caused Goldman, Sachs & Company to deliver to the bankrupts bullion instead of checks, Goldman, Sachs & Company would of necessity have had to accompany the bullion with the same information "for whose account" it was being paid.* In these latter circumstances it could not seriously be argued that the *money* delivered to the bankrupts under instructions that it was "for account of" Latzko and Popper was being transmitted for collection or otherwise restrictively—or other than as a deposit creating a debtor and creditor relationship. The mere fact that the payment was made by check of Goldman, Sachs & Company and was accompanied by a letter designating the account for whose benefit the payment was made cannot change the result.

A.

The Inapplicability of White vs. Miners National Bank, and Similar Cases.

The main argument advanced by the petitioners and the court below to justify their ignoring the rule of the *Burton* case is that, in a line of cases involving one form of restrictive *endorsement* and not dealing at all with the banking transaction here involved, the words "for account of" have been held by Courts to result in an agency relationship. That argument is the same as was unsuccessfully advanced in several recent cases in this Court* such argument being in effect that a word or phrase used under one set of circumstances always must have the same meaning even when used under wholly different circumstances and with a wholly different purpose.

Assuming, however, for the moment, that cases relating to endorsements have any relevancy at all to the problem presented by the present set of facts, the distinction between those cases and the rule to be applied in the present case is recognized by the Negotiable Instruments Law itself.

Section 66 of the Negotiable Instruments Law of the State of New York (Laws 1909, Chapter 43), which is Section 36 of the Uniform Negotiable Instruments Act, provides:

> "Sec. 66. *When indorsement restrictive.* An indorsement is restrictive, which either:

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*U. S. vs. *Chamberlin*, 219 U. S., 250, 262; *Price* vs. *U. S.*, 269 U. S., 492.

1. Prohibits the further negotation of the instrument; or

2. Constitutes the indorsee the agent of the indorser; or

3. Vests the title in the indorsee in trust for or to the use of some other person.

But the mere absence of words implying power to negotiate does not make an indorsement restrictive."

And Section 67 of the New York Act (Section 37 of the Uniform Act), provides as follows:

"Section 67. *Effect of restrictive indorsement; rights of indorsee.* A restrictive indorsement confers upon the indorsee the right:

1. To receive payment of the instrument;

2. To bring any action thereon that the indorser could bring.

3. To transfer his rights as such indorsee, where the form of the indorsement authorizes him to do so.

But all subsequent indorsees acquire only the title of the first indorsee under the restrictive indorsement."

From the foregoing sections, it is apparent that restrictive endorsements fall into two classes:—

(a) Those for the benefit of the endorser himself; and

(b) Those for the benefit of a third person.

Where an instrument drawn by A to the order of B is endorsed by B to C for account of B or for B's benefit,

then the rule is settled that B, the endorser, constitutes C merely the agent of B, and that neither the legal nor the beneficial title passes to C and that C becomes merely the agent of B to collect the instrument. In legal effect, the instrument is *a mere power.*

Where, however, an instrument drawn by A to the order of B is endorsed by B to the order of C for account of or for the use of D, then the rule is that B intends to and does divest himself of all legal title and that C obtains the legal title to the instrument which he holds *prima facie* for the use of D.

Hook vs. *Pratt,* 78 N. Y., 371.

But in this second class of cases, it is apparent that the question remains open as between the endorsee (C) and the third party (D), whether C, the endorsee, takes not only the legal title, but as against D, also the beneficial title. That question is one which depends wholly upon the arrangement which, in fact, exists between C and D. If by agreement, express or presumed, they have arranged that upon the receipt of this type of instrument, both legal and beneficial title shall pass to C and that a mere debtor and creditor relationship shall spring up, that is no concern of B who has divested *himself* of all interest in the instrument. If, in fact, no such agreement has been made, either expressly or by a course of conduct, or by any other method, then, of course, C would hold the proceeds for the use of D.

With these fundamental distinctions in mind, it becomes apparent that even if the principles underlying the restrictive endorsement cases are at all relevant

here, the cases relied upon by the petitioners are not inconsistent with the contentions of the respondent.

The petitioners and the court below relied mainly, if not entirely, on a line of cases which have as their original authority the decision of this Court in *White* vs. *Miners National Bank* (1880) 102 U. S., 658. An analysis of the *White* case, which is for this purpose an analysis of all of the cases following it, and a comparison of its facts with those of the present case furnishes the best illustration of why those decisions are inapplicable to the present circumstances and why the District Court was correct in holding that the checks in the present case had *not* been deposited for collection. In the *White* case the Miners Bank, the payee, by its president Brownell, endorsed drafts to the plaintiff White in the following manner:

> "Pay S. V. White or order for account Miners Bank, Georgetown, Colorado. J. L. Brownell, P't."

White paid the bank the amount of the drafts less a discount, and when the drafts were not paid at maturity sued the bank both on its endorsement and for money paid to the bank's use. The decision of this court was that the plaintiff might recover on its second count for money paid but in the course of its opinion, at page 661, it stated that:

> "It seems to us that the Court below correctly construed the effect of the endorsement to be to make White the agent of the bank for the collection of the money."

But in the *White* case, as in all of the other cases relied upon by the petitioners, the endorser endorsed to the endorsee for the *endorser's benefit,* and therefore intended to constitute the endorsee the endorser's agent to collect the drafts—a mere power—an endorsement of the first class under New York N. I. L., Sec. 66, quoted *supra.* Under these circumstances, neither legal nor beneficial title passes to the agent. *In none of these cases, however, was the question presented as to the respective rights of the endorsee and the third party for whose account the endorsement was made*—an endorsement of the second class under Sec. 66. In all the cases relied on by petitioners, the question was either as to the respective rights of the endorser and endorsee, or of the endorsee or a subsequent holder, as against the maker. In none was there a presumption, such as here exists, of the actual relation between the endorsee and the third party. In none was the instrument drawn at the instigation of the endorsee.

Again, in the *White* case, as in all of the cases relied upon by petitioners, the defendant-endorser had no account with the endorsee (White) for which "account" the endorsee received the drafts and to which "account" the amounts of the drafts were to be credited. The natural and reasonable construction of the endorsement in those cases was that the endorser (Miners Bank) intended to constitute the endorsee (White) its agent to collect the drafts from the third party drawees. Just as in the present circumstances the use of the words "for account of" could not have been avoided if the bankrupts were to be instructed for what purpose the pay-

ments were being made to them, so in the *White* case the use of the words "for account of" could have had no other meaning or purpose than to constitute the endorsee an agent for collection. In the *White* case the words did not have to be used to explain the source of the payment inasmuch as the transaction was between the only two interested parties. There was no payment by a third party for *another's* "account" which required explanation.

B.

The Parole Evidence Rule would not be violated, as claimed in Petitioners' Point I, if the circumstances surrounding the delivery of the check were investigated to determine the meaning of the phrase "Favor Of".

The petitioners contend in their Point I that because the phrases "for account of" "for collection," etc., have a settled meaning in the ordinary restrictive endorsement cases it would be a violation of the parole evidence rule to consider the circumstances surrounding the delivery of the checks here in question as a basis for determining the legal relationships resulting from such delivery. Petitioners' contention is unsound for three reasons.

1. *The very facts upon which respondent relies and which were relied upon by Judge Augustus Hand in the District Court* (fols. 117 to 118) *and by the Special Master in interpreting the meaning of the terms "for account of" or "favor of" were allegations contained in petitioners' own reclamation petition and facts offered*

in evidence by petitioners themselves. Judge Hand said (fol. 119) that "the effect sought to be given here to the words 'for account of' is contrary to the natural meaning of the words under the circumstances" by reason of the fact that "here the deposit was in the claimant's ordinary checking account. Instructions to place it in such account emanating from them, and due to the necessity of indicating from whom the check was received, create a different situation than that in *White* vs. *Miners National Bank*" (fol. 118).

The fact that the deposit was in the petitioners' ordinary checking account and the fact that instructions to place it in such account emanated from petitioners were facts *pleaded and proved by the petitioners. Indeed the Record contains no evidence of any kind, written or parole, offered by the respondent as to the meaning of "for account of."* The only evidence of any kind in the entire case, in the introduction of which the respondent had any part, was the evidence that the bankrupts credited petitioners with the amounts of the checks upon the days when the checks were received and that the American Exchange National Bank in turn credited the bankrupts when the bankrupts deposited the checks with that bank. Even these facts were not offered by the respondent alone but were put into the Record upon the joint stipulation of both parties (fols. 72 to 75). On such a Record this Court will not permit petitioners to assert here that the Special Master and the Court below were foreclosed from interpreting the meaning of the term "favor of" *in the light of the very facts adduced by the petitioners' own evidence.*

2. As a correlary to the foregoing, and since the respondent introduced no evidence whatsoever, except as above noted, the Record of course contains not a single objection or exception taken by petitioners to any evidence offered. *No exception having been taken petitioners cannot now be heard to object to the evidence introduced.* (See opinion of Learned Hand, D. J., in *Re Brown,* 189 Fed., at 437).

3. While the aforesaid two reasons dispose of petitioners' contentions it is equally apparent that they would be untenable if the evidence in question had been offered by the respondent and had been excepted to in a timely manner by petitioners for it has long been a well established limitation to the parole evidence doctrine that

> "In order to ascertain the relation of the words of a document to facts, every fact may be proved to which it refers, or may probably have been intended to refer, or which identifies any person or thing mentioned in it. Such facts are hereinafter called the 'circumstances of the case.' "
>
> *Chase's Stephen's Digest of the Law of Evidence* (Second American Edition, 1910), 229.

Wigmore, after tracing the development in the law away from the originally absolute parole evidence rule and the tendency toward the enlightened view that no document is complete in itself but must be read in the light of the circumstances under which it was executed,

states at page 3499, Section 2470 of his work on Evidence (1905):

> "The truth had finally to be recognized that words always need interpretation; that the process of interpretation inherently and invariably means the ascertainment of the association between words and external objects; and that this makes inevitable a free resort to extrinsic matters for applying and enforcing the document. 'Words *must* be translated into things and facts.' Instead of the fallacious notion that 'there should be interpretation only when it is needed,' the fact is that there must always be interpretation. Perhaps the range of search need not be extensive, and perhaps the application of the document will be apparent at the first view; but there must always be a travelling out of the document, a comparison of its words with people and things. The deed must be applied 'physically to the ground.' * * * Once freed from the primitive formalism which views the document as a self-contained and self-operative formula, we can fully appreciate the modern principle that the words of a document are never anything but indices to extrinsic things, and *that therefore all the circumstances must be considered which go to make clear the sense of the words,—that is, their association with things.*"

The quotations from *Wigmore* and *Chase* merely summarize the now established principle that in interpreting a written instrument extrinsic evidence of the "circumstances of the case" is admissible.

This is really no exception at all to the parole evidence rule. Parole evidence is not being considered to

controvert the meaning of the instrument. The circumstances surrounding it are simply examined to explain it. Thus in the present case the Special Master and the Court quite properly considered not only the checks themselves and their covering letters, but also the "circumstances of the case",—the fact that the petitioners maintained an "account" with the bankrupts; the fact that it was the petitioners who "caused" the three New York banks and bankers to deliver checks to the bankrupts, and the fact that, unless the banks and bankers had designated the account on bankrupts' books to be credited, bankrupts would not have known whom to credit.

Further authorities on this subject need not be here considered but reference is made to respondent's analysis at pages 35 to 38 of its brief in the *Rochling* case, No. 34, of the cases of

United States vs. *Bethlehem Steel Company* (1906), 205 U. S., 105;

Middleworth vs. *Ordway* (1908), 191 N. Y., 404;

Central Coal & Coke Co. vs. *Good & Co.*, 130 Fed., 793, 799.

The cases cited hold that words used in one set of circumstances need not have the same meaning as the same words used in different circumstances.

As said by this Court in *United States* vs. *Chamberlin*, 219 U. S., 250, 262, in construing the meaning of the word "debt":

> "A tax may or may not be a 'debt' under a particular statute, according to the sense in which the word is found to be used."

And in the same case, after distinguishing certain earlier cases where the word "debt" was held not to include a tax, the Court said that in those cases "the context forbade the conclusion."

> *Accord, Price* vs. *U. S.*, 269 U. S., 492, bottom 501.

And so here, therefore, the meaning of the words "for account of" or "in favor of" must depend upon the "sense in which the word is found to be used." Because in the endorsement cases an endorsement by B to C for account of B makes C an agent, with power to collect, and because in that class of cases perhaps a "contrary conclusion" is forbidden, that fact is of little aid in determining in what sense similar words are used where a depositor causes a deposit to be made in his own account and his bank is notified by a notation or memorandum that such deposit is in effect "for the account of" the depositor giving such instructions.

Conclusion to Point II.

In summary then, in the present case, the rights of the petitioners (not endorsees) are being considered and it is third parties, to wit, the *New York banks,* who used the allegedly restrictive words. Furthermore, in all the other cases which deal with *endorsements,* the only conceivable reason for the use of the word "for account of" was to create the endorsee a fiduciary, whereas in the

present case, as has already been pointed out, *even if no fiduciary relationship was intended,* there would have been no other way for the New York bank to indicate the person to be benefited by the payment other than by the use of such or similar words. Nor did the New York banks have the right to determine as between the bankrupts and the petitioners the effect of the deposit of the checks. *There is nothing in common between the circumstances of the present case and those of all of the other cases relied on by the petitioners, other than the simple fact that the same words "for account of" were used.*

POINT III.

The Court below erred in holding that the bankrupts took the National City Bank check for $1,294 in any different capacity than they took the Goldman Sachs check for $15,000.

As already pointed out in the preliminary statement on page 8, after having correctly concluded that the use of the words "for account of" in the letter accompanying the Goldman Sachs check was merely to indicate the account to be credited, with the result that the bankrupts took title to that check, the court then erred when it reached a different conclusion with respect to the National City Bank check where the words "in favor of" appeared on the face of the check. The cause of this error was the court's confusion in believing that the words on the face of the check, since they might have

affected the rights of transferees of the check, were at all material so far as petitioners' rights were concerned. Obviously this is error for, as already pointed out, in considering the relative rights of the petitioners and the bankrupts, the effect of notice to third parties and the rights of such third parties is unimportant.

That this was the reason for the court's reaching different conclusions in the two cases appears clearly from Judge Roger's Opinion (fol. 229). He said:

> "The petitioners alleged in their petition that on June 15, 1923, they caused the National City Bank of New York to deliver to the bankrupts this check to be collected for the account of the petitioners, and that it was to be so collected appears on the face of the check itself. For the words "Favor N. Latzko and A. Popper, Budapest," seem to us, on the whole, not to differ in effect from "Collect for N. Latzko and A. Popper, Budapest." *A check so drawn cannot be said to be freely* NEGOTIABLE. Any payee *to whom it was indorsed* would take the proceeds when collected not for himself but for N. Latzko and A. Popper."

It is obvious from this quotation that the court was not considering the question here presented, i. e., the relationship between the bankrupts and their depositors, the petitioners. The court was confusing the question actually presented with one involving the effect that the phrase "in favor of," when appearing on the face of a check, might have *on a subsequent endorsee* of the bankrupts (their bank, the American Exchange National Bank, for instance). It might be that the appearance of such a phrase on the face of a check would put an en-

dorsee such as the American Exchange National Bank on notice to inquire what *in fact* was the relationship between the endorser and the person for whose "favor" the endorser had received the check. If no such inquiry were made and the endorsee bank gave credit to its endorser it might do so at the risk of learning later that as a fact the check belonged not to the endorser but to that other person for whose favor the endorser had received it. Here, however, such inquiry would have established *the fact* that the bankrupts had acquired title to the check.

So far as the payee endorser himself was concerned, however, the phrase in question does not constitute notice, for the instructions of the transmitting bank, in this case the National City Bank, cannot effect the actual relationship existing between the payee, the bankrupts in this case, and their depositors, the petitioners.

That the Circuit Court of Appeals misapprehended the problem and that it was considering the possible rights of subsequent endorsees rather than the relationship between the bankrupts and petitioners is further substantiated and almost conclusively proven by the distinction recognized by that court between the case where the phrase "favor of" appeared on the face of the check and where it did not. *If the phrase was notice to the bankrupts of anything, it was just as much notice to the bankrupts whether it appeared on the face of the check or in a covering letter to them.* The only additional effect which would result from the appearance of the phrase on the face of the check is, as the Court itself stated, in connection with its "negotiability;" i. e., the

notice which it might give to subsequent endorsees. The rights and liabilities of such subsequent endorsees are not presented here and yet it is clearly their rights and liabilities that the Circuit Court was considering, for, at folio 230, in considering the effect of the appearance on the face of the check of the phrase "N. Latzko and A. Popper Budapest" it said:

> "A check so drawn cannot be said to be freely *negotiable.* Any payee *to whom it was endorsed* would take the proceeds when collected not for himself but for N. Latzko and A. Popper."

The use of the word "negotiable" and the consideration of the effect of "endorsement" was what the Court had in mind. It is true that the Court referred to any "*payee* to whom it was endorsed" but that simply indicates a further confusion. A payee's rights do not depend on endorsement.

That as between the bankrupts and the petitioners the use of the words "in favor of" on the face of the check did not constitute the bankrupts agents for collection but established a debtor and creditor relationship upon the credit of the check to the petitioners' account, has already been shown by the discussion in the previous points. The only answer made by the petitioners to this argument is its discussion of the cases of which *White* vs. *Miners National Bank* is typical. The inapplicability of the doctrine of those cases to the transactions here involved has already been sufficiently discussed in Point II and need not here be repeated.

POINT IV.

The judgment of the Circuit Court of Appeals should be affirmed insofar as it denies the petitioners' right of reclamation to the proceeds of the Goldman Sachs check and should be reversed insofar as it granted the petitioners' reclamation claim to the proceeds of the National City Bank check.

Respectfully submitted,

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